Written Testimony of
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Chairman Stevens, Co-Chairman Inouye, and members of the Committee, my name is Dan Fawcett and I am the Executive Vice President, Business and Legal Affairs and Programming Acquisition, at DIRECTV, Inc. Thank you for inviting me to testify today on video competition, program access, local sports programming, and the threats to competition arising from the proposed Adelphia transaction.

A key development in the American economy over the past twenty years has been the rise of a competitive video marketplace. Today, competition means consumers have more choices; customer service and pricing are becoming more responsive; technological innovation is flourishing, and tens of thousands of jobs have been created.

This is no accident. Rather, it is the direct result of public policies that promote competition. But today, this progress is being threatened.

Comcast and Time Warner, the nation's two biggest cable companies, intend to divide Adelphia's subscribers between them and to swap many of their current subscribers. If allowed to do so, Comcast and Time Warner will control access to approximately 6 in 10 of the nation's cable subscribers and almost half of all pay-TV subscribers. Of greater concern, the proposed transaction will create concentrated regional monopolies across the country where one of the two companies will become *the* single dominant video provider.

If allowed to establish such regional monopolies, without adequate safeguards, I can assure you that Comcast and Time Warner will deny key regional programming – especially local sports – to their competitors. Maybe they will do so directly, because the program access rules will not prevent them. Or maybe they will do so indirectly by increasing the price of this programming, which the program access rules also allow. Either way, tens of millions of consumers will be harmed, and fair competition will be impossible.

I know this because I've seen it all before. My job at DIRECTV is to negotiate carriage deals with programmers, including the regional sports networks ("RSNs") that carry teams like the Indians and the Mets and the Red Wings in their hometowns. Over the years, I've seen how cable operators have managed to deny their competitors local sports programming in places like Philadelphia, where DIRECTV subscribers *still* cannot watch the Phillies, 76ers, and Flyers; and Chicago, where the price DIRECTV pays for sports programming has increased at exorbitant rates.

This should not be the model for the rest of the country. To prevent this, we have asked the FCC to place safeguards on the Adelphia transactions and we also urge Congress to update and strengthen the program access rules. Taken together, these regulatory and legislative recommendations will help to ensure that the competitive video marketplace that exists today will continue to flourish in the future.

I. WHERE CABLE OPERATORS HAVE GAINED SUFFICIENT REGIONAL CONCENTRATION, THEY HAVE WITHHELD OR RAISED THE PRICE OF KEY LOCAL SPORTS PROGRAMMING

Not so long ago, there was no such thing as video competition. If you wanted multichannel programming, your local cable operator was the only place to go. Over the past 15 years, however, sound public policy decisions by Congress have helped foster the rise of a truly competitive video marketplace. With DIRECTV taking the lead, DBS has grown from fewer than 10 million subscribers in 1999 to more than 26 million today – proof that when it comes to video, Americans want choice.

Thanks to this increased competition:

- DIRECTV and others have invested billions in new innovations.
- DIRECTV itself has invested billions to make local broadcast signals available to more than 93 percent of television households, and is investing billions more to create the capacity to provide 1500 high definition local broadcast channels.
- Customer service and choice have improved throughout the video industry.
- Rural customers now have access to the latest products and services.

Because of the competitive marketplace this Committee helped create, *all* Americans – not just DIRECTV subscribers – are enjoying a better television experience.

But it almost never happened. Some Members of this Committee may remember that, when satellite first appeared on the scene, cable responded as any monopolist would – by trying to protect its monopoly. One strategy was to deny key programming to its satellite rivals.[1] Cable hoped that, if it could prevent satellite from carrying the most desirable programming services, it could strangle competition in its infancy. So cable operators refused to sell programming they controlled to satellite and used their market power to secure exclusive contracts with key unaffiliated programmers.

But to cable's chagrin, Congress stepped in. In 1992, Congress created program access requirements designed to prevent such abuses of market power. Under these rules, cable operators were prohibited from negotiating exclusive or "sweetheart" deals for cable-affiliated programming. The idea was that, with a level competitive field, new entrants such as DIRECTV could compete on the merits of their offerings, and consumers would benefit from their efforts to win customers from each other. The rules have been an unmitigated success: without them, satellite television would never have gotten off the ground.

In recent years, however, cable operators have devised increasingly sophisticated ways around Congress's pro-competitive rules. The program access rules no longer provide any real barrier to cable giants such as Comcast and Time Warner. Thus, we now find ourselves in much the same situation as before Congress enacted the program access rules – in regions where a cable operator possesses market power, it will deny or raise the price of key programming to its competitors. In particular, cable will seek to withhold

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1 This, of course, wasn't the only strategy employed by cable to retain its monopoly. Some Members of this Committee might remember "Primestar," the cable industry's attempt to launch its own satellite service as a "stalking horse" to block competitive DBS entry – in part by obtaining scarce DBS licenses. In the end, the Department of Justice and 45 states sued Primestar and obtained a consent decree curbing the most obviously anticompetitive tactics.

the kind of local sports programming that the FCC has determined to be "must have" for distributors.

Let me give you some examples:

A. Pure Withholding of Affiliated RSN – Comcast in Philadelphia

The poster child of local sports withholding is, of course, Philadelphia. Because Philadelphia is Comcast's hometown, Philadelphia was one of the first "clustered" markets. While some metropolitan areas are served by many different cable operators, Philadelphia is served almost exclusively by Comcast. Armed with such regional market power, Comcast created "Comcast SportsNet" – an RSN with rights to the Philadelphia Phillies, Flyers, and 76ers. It then decided not to make this network available to Comcast's competitors.[2]

It was able to do this because of what has since come to be known as the "terrestrial loophole." The program access rules only apply to programming delivered to cable systems *by satellite*.[3] Because it delivers Comcast SportsNet to its cable systems via fiber, Comcast argues that Comcast SportsNet is not subject to the program access rules and need not be made available to customers of their competitors.

[2] In 2002, the last time Comcast had a big merger pending, it was persuaded to make Comcast SportsNet available to cable overbuilders such as RCN. But it has never made this programming available to satellite.

[3] When Congress was drafting the program access provisions in 1992, it wanted to allow exclusive deals for local cable news channels. The idea was that, if a cable system spends a lot of money creating a local cable news channel, it shouldn't have to make that channel available to its competitors. At the time, local cable news was primarily delivered to cable offices over telephone wires. Other programming (such as ESPN, CNN, etc.) was delivered to cable offices via satellite. So Congress decided to restrict exclusive contracts only for "*satellite* cable programming" (that is, "video programming which is transmitted via satellite").

DIRECTV has always thought this was, at best, an evasion of the 1992 Cable Act. But the FCC (and, later, the DC Circuit) concluded that a plain reading of the statute's reference to "satellite programming" allows Comcast to freeze out its competitors in Philadelphia. And this is exactly what Comcast has done. To this day, fans of the Phillies, 76ers, and Flyers must either give up the right to root for their home teams or give up their right to subscribe to the video provider of their choosing. Is it any wonder that satellite's market share in Philadelphia is less than half of what it is nationally?

B. Pure Withholding of Unaffiliated RSN – Time Warner in Charlotte

Comcast found it easy to deny satellite subscribers local sports programming in Philadelphia because it owned the RSN in that market. But cable doesn't need to own a sports channel in order to deny it to satellite subscribers – just ask DIRECTV subscribers in Charlotte.

In Charlotte, Time Warner controls a regional monopoly similar to that enjoyed by Comcast in Philadelphia. In fact, Time Warner controls so many subscribers in Charlotte that, when Carolina Sports and Entertainment Television ("C-SET") launched last season with rights to the NBA's Charlotte Bobcats, Time Warner was able to establish an exclusive deal to carry the team's games. Because C-SET was not affiliated with a cable operator, the program access rules did not prohibit this exclusive deal. Since then, C-SET has gone out of business. But just a few months ago, Time Warner secured yet another deal with the Bobcats (this time without C-SET). And the Bobcats are still not available to satellite. And so here too, as in Philadelphia, local fans face the same grim choice: give up watching the team, or give up the right to choose video providers.

C. Uniform Price Increases – Comcast in Chicago

Cable operators have found that refusing to sell local sports programming to competitors, although effective in boosting market share, is a fairly blunt tool. Savvy cable operators have thus resorted to more subtle – but equally anticompetitive – tactics.

Take Chicago, for example. In 2002, Comcast purchased AT&T, and in the process established a regional monopoly in Chicago similar to its dominance of Philadelphia (and similar to the level of concentration that the Adelphia acquisition could create in markets across the country). Comcast next purchased the rights to the Bulls, Blackhawks, Cubs and White Sox and launched its own sports network, CSN Chicago. When DIRECTV sought carriage of this critical programming, Comcast made it available to DIRECTV – but at double the price DIRECTV had been paying to carry these same games. Unwilling to forgo this must-have programming, DIRECTV had no choice but to accede to Comcast's demands.

The program access rules do not prohibit this kind of behavior so long as Comcast pays the same high price. But that restriction is of no concern to Comcast because even inflated payments are simply a transfer of money from one division of Comcast Corporation to another.

Comcast thus has every incentive to jack up the price of CSN-Chicago (and similar RSNs) in the future. If DIRECTV doesn't pay the higher prices, Comcast gets a *de facto* exclusive for the channel. If on the other hand DIRECTV pays the artificially high price, Comcast extracts a supra-competitive rate and drives up DIRECTV's costs. This, in turn, makes it more difficult for DIRECTV to compete with Comcast on price. Either way, Comcast wins – and consumers lose.

D. "Stealth Discrimination" of Affiliated RSN – Comcast in Sacramento

Sometimes, a cable operator with a regional monopoly doesn't even need to "officially" raise RSN prices in order to distort competition. In Sacramento and San Francisco, as in Chicago, Comcast was able to establish a regional monopoly when it purchased AT&T's cable systems. And, as in Chicago, it went out and created its own Sacramento RSN, CSN West, with rights to only *one* professional team, the Sacramento Kings.

In my experience, RSNs only offer their programming in the territory established for the team by its league. But this is not the case for CSN West. Comcast has mandated a service area for CSN West much larger than the area in which the NBA permits CSN-West to carry Kings games. Under Comcast's pricing scheme, however, DIRECTV must pay for subscribers to whom it can't even show the Kings games. In fact, DIRECTV pays for more subscribers who cannot watch the games than those who can. These customers account for one-third of the total license fees paid for the network. Cable operators, with much smaller service areas, do not face this dilemma.

E. The Trend Continues . . .

One might think that, with a gigantic merger pending before the FCC and the FTC, Comcast and Time Warner might at least slow down their effort to undermine competition through the acquisition and withholding of sports programming. But even the threat of government oversight does not appear to faze them.

Time Warner stands to gain enormous market share in Ohio through the Adelphia transactions. So it recently announced that it will help launch a new RSN to carry Cleveland Indians games. Following the playbook used by Comcast in Chicago, Time Warner has proposed a rate for this single-team, part-time channel that is almost 90 percent of what DIRECTV was paying for *four* teams: the Indians, Cavaliers, Reds *and* Blue Jackets.

Time Warner and Comcast are trying to do the same thing in New York, where they control many subscribers. Both have an ownership interest in SportsNet New York, the new Mets channel. SportsNet New York wants to charge DIRECTV a higher price than it pays on a per game/per subscriber basis for the YES network – which carries the Yankees. This is an astronomical rate, particularly considering the fact that the ratings for the Mets games on Fox Sports New York/MSG have historically been less than *half* the ratings for the Yankees games on YES.

Again, Comcast and Time Warner have nothing to lose by this behavior. They can set "nondiscriminatory" high prices, knowing that they will recoup the cost through their ownership interest in the RSN. If DIRECTV refuses to go along, DIRECTV subscribers will lose Indians and Mets games. For Clevelanders and New Yorkers who want to watch their local teams, DIRECTV will not be an option, to the delight of Comcast and Time Warner. If, on the other hand, DIRECTV pays the inflated price, our costs go up. Again, Comcast and Time Warner win, and consumers lose.

II. THE ADELPHIA TRANSACTIONS WILL MAKE THIS BEHAVIOR POSSIBLE IN MANY MORE MARKETS

There is one constant in each of the scenarios I've just described to you. In Philadelphia and Charlotte and Chicago and Sacramento, a single cable operator enjoys a very high market share. Thus, Comcast could only withhold Philadelphia sports programming because it controls a regional monopoly in Philadelphia. And it could only raise the price of sports programming in Chicago after it gained a regional monopoly there in 2002. This is for a simple reason – as a cable operator controls more subscribers in a particular area, an RSN operating in that area gains more from distribution on the cable system and *loses less* if it denies distribution to the cable operator's rivals.

This is why the proposed Adelphia transactions are so dangerous. Comcast and Time Warner propose to split up Adelphia's systems, and swap systems among themselves, for the stated purpose of increasing regional concentration. Indeed, they are *selling* this merger both to Wall Street and to regulators as one that will increase what they call "geographic rationalization."

One way to measure the extent of concentration that will result from this merger is through a tool called the Herfindahl-Hirschman Index ("HHI"), a widely used and accepted measure of market concentration. Under the Department of Justice Merger Guidelines, a merger resulting in an HHI greater than 1800 and a change of more than 100 is presumed to create market power. As described in the table below, the HHI's resulting from this transaction would dwarf those thresholds in the pay-TV markets in many RSN service areas.

RSN	HHI	HHI Change
C-SET	4,210.6	403.7
Comcast SportsNet Philadelphia	4,156.7	376.9
FSN Florida	2,529.2	580.7
Sun Sports	2,515.2	578.0
FSN Ohio	2,395.7	837.8
FSN West/West 2	2,216.9	740.5
Mid-Atlantic Sports Network	2,168.7	358.6
Comcast/Charter Sports Southeast	2,148.6	325.8
Comcast SportsNet MidAtlantic	2,126.4	390.8
FSN Pittsburgh	2,080.1	576.9

In terms of market share, this means that Comcast will have over 75 percent of pay-TV subscribers in the Boston DMA, 70 percent in Pittsburgh, and 67 percent in West Palm Beach. Time Warner's share in Los Angeles will go from 9 percent to 48 percent and in the Cleveland, Cincinnati and Columbus pay-TV markets, Time Warner's market share will be 60 percent or more.

Think about what this means. In markets such as Philadelphia, Chicago, and Charlotte where Comcast and Time Warner already have regional monopolies, they have withheld sports programming from competitors or raised its price to competitors. With the Adelphia transaction, Comcast and Time Warner seek to create the conditions that would allow them to do the exact same thing in Boston and Pittsburgh and Cleveland and Los Angeles and West Palm Beach. Which means fans of the Red Sox , the Pirates, the Indians, the Cavaliers, the Dodgers, and the Clippers could all find themselves over a barrel – forced to either give up the right to watch their home town teams or give up the right to choose video providers. With the number of markets affected by the Adelphia transaction, this threatens the progress Congress set in motion over a decade ago.

III. The FCC should Impose Conditions on the Adelphia Transactions

If Comcast and Time Warner are successful in their plans, we could be looking at a return to the "bad old days" of cable monopoly. DIRECTV has thus asked the FCC to impose narrowly-tailored conditions on the proposed Adelphia transactions. These recommendations closely mirror the conditions imposed by the FCC in the News Corporation/DIRECTV merger.

First, the FCC should prohibit exclusive deals (including "cable only" exclusives) for RSNs, regardless of delivery mechanism or affiliation, in the regions where the Adelphia transaction will create market power. This will prevent Comcast and Time Warner from taking advantage of the "terrestrial loophole" (as Comcast has done in Philadelphia). It will also prevent Comcast and Time Warner from entering into exclusive deals with unaffiliated RSNs in highly concentrated markets (as Time Warner has done in Charlotte).

Second, the FCC should prevent "price discrimination" by permitting distributors to seek arbitration when negotiations break down. This would simply allow a competitor to seek an independent third party review to ensure nondiscriminatory and fair pricing to competitors. An integral component of this recommendation is that competitors must be permitted to continue providing this "must have" programming to consumers while any arbitration is pending.

These conditions are not exceptional in the video service industry. In fact, the FCC has consistently noted that the rise of regional monopolies poses a threat to competition and that it is appropriate to exercise regulatory authority to prevent such monopolies from exercising their market power to the detriment of competition.

Only through these narrow conditions can the FCC address the very real anticompetitive consequences of the merger that I have described to you. I would thus ask this Committee to urge the FCC to approve this transaction only with these or similar safeguards.

IV. CONGRESS SHOULD RE-EXAMINE THE PROGRAM ACCESS RULES

For those concerned about competition in the video market, the Adelphia transactions are plainly the immediate priority. In the longer term, however, Congress should consider re-examining the program access rules. In particular, it should close the terrestrial loophole and ensure that the rules apply to the other forms of discrimination I have described.

As discussed above, the terrestrial loophole allows cable operators to deny programming from their competitors so long as the programming is not delivered to the cable systems. The rationale for this was to encourage cable operators to develop their own local news channels. The exception certainly was never intended to apply to local sports programming, which was delivered at the time via satellite. There is, moreover, simply no need for Congress to encourage the creation of local sports programming. Such programming, as the FCC has determined on several occasions, is among the most valuable on television. It also cannot be "created" through Congressional encouragement – each team is unique, and games involving that team cannot be duplicated in the way that, for example, local news can.

When it created the program access rules, Congress surely never expected regional sports programming to be subject to exclusive deals. Congress should remedy this by closing the terrestrial loophole (at least as for RSNs), and make it clear that the full panoply of the program access restrictions in the 1992 Cable Act apply to RSNs, however they may be delivered to cable systems.

When it examines the program access rules, moreover, Congress should also consider how to address the other sorts of anticompetitive activities that I have described, but that the existing rules appear not to reach. There is simply no reason why cable operators should be allowed to engage in the kind of behavior exhibited by Comcast in Chicago and Sacramento. It should also ensure that the program access rules will continue to apply beyond their current expiration date.

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Cable operators were once the only game in town. As a result, prices were high, choices were limited, customer service was legendarily bad. But, at least in most places, competition is now the order of the day and the results are remarkable: unprecedented innovation, service improvements, more responsive pricing and more choices than ever before.

But all that has been gained could yet be lost. If allowed to proceed with the Adelphia transaction without adequate safeguards, Comcast and Time Warner will have both the incentive and the ability to undermine competition in market after market throughout the country. This will undo the progress Congress set in motion with the program access rules over ten years ago. On behalf of the tens of millions of consumers who want continued access to their local teams at reasonable prices, I ask you not to let that happen.

Chairman Stevens, Co-Chairman Inouye, and Members of the Committee, thank you for allowing me to present DIRECTV's views on these important matters. I would be happy to take your questions.